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ANOMALOUS INDORSEMENT IN PENNSYLVANIA.

When one, not a payee or maker, indorses a note for the purpose of giving the maker of it credit with the payee, and before the note has been indorsed by the payee, he is called an anomalous indorser. It is the impression, in Pennsylvania, that there is no way in which to hold such an indorser. A wishes to borrow \$1000 and B offers to lend it if A will give security. Accordingly a note is made—payable to B, signed by A as maker, and indorsed by C to give it credit with B, who then parts with his \$1000 to A. The attitude of the Pennsylvania courts, it is thought, is : that B cannot hold C ; that a subsequent holder who has notice of the circumstances of the indorsement cannot hold C ; and that it is sufficient notice of these circumstances if B's name appears on the back below C's. A doctrine of this sort is admitted to be not altogether satisfactory ; for, in the first place, it is opposed to the law of, perhaps, every jurisdiction in which negotiable instruments are in use ; and because, secondly, it is a result which our sense of natural justice instinctively condemns ; but still it is reinforced by a respectable opinion that on principle it is correct and that any contrary doctrine is not. Under such circumstances two questions are naturally suggested. Is it really inconsistent with the legal theory of notes to hold an anomalous indorser ? And if not, have the cases, nevertheless, settled the question beyond hope of being corrected ?

The first question has been so much discussed that one need not attempt to add anything to what has already been said upon it. My purpose in going into it is to get together some material that will be of help in answering the second, that is, in clarifying the cases, and so to find out exactly on what terms Pennsylvania really is with the subject.

Putting the intimation already thrown out into the shape of a proposition, we may start out by saying that it is *not* inconsistent with legal theory to attach a liability to an anomalous indorser ; and since, to prove this, it is obviously necessary to

show only *how* he can be held, lack of patience drives us at once to the consideration of this narrower question. Now, however much we may be bent upon holding him to some liability, we will quickly make up our minds not to hold him to a liability that does not fit his intention. It is unfair, for instance, to hold him as a maker or guarantor, for he did not intend to assume the liability of either of these. He intended to be liable only after the maker; and, although he understood himself to be liable secondarily, it was not necessarily as a guarantor. He expected, furthermore, to be liable only upon demand and notice; to make him a maker or guarantor dispenses with these. Pennsylvania, in the early cases, did not notice these objections and the disposition to hold him as a guarantor was almost crystallized into a settled doctrine. Of course, there was no injustice in those cases in which there was notice; and one is not disposed to object seriously to a case which it is better to know is settled than how. But the mistake led to holding the indorser even where there was no notice and so imposed a different liability from what was assumed. Both these errors were soon unconsciously corrected by the Statute of 1885, which not only required guaranties to be in writing, but did not have that requirement satisfied by simple indorsement. Corrected? Yes, but not entirely; an opportunity was open to start on the right track. Instead, the courts made another and more serious mistake; they assumed that if the anomalous indorser could not be held as guarantor, he could not be held at all—this without really any attempt whatever at hunting for another liability.

Why not hold him as an indorser? That certainly is the very liability he intended to assume, and, besides, demand and notice are necessary to hold him as such; so that the objections that keep him from being responsible as a maker or guarantor are got rid of. It has, therefore, been suggested that he should be held as a first indorser, because “the prior party’s position on the note seems to render his liability strictly analogous to that of the drawer of a bill upon the maker in favor of the payee.”¹ There is something clumsy in

¹ Daniel, Sect. 714.

this suggestion and, besides, no one but a payee can be first indorser.

A better and more scientific theory, it seems, has been adopted by the New York court. The payee, as holder, is allowed to sue the anomalous indorser as second indorser, and the objection that he cannot recover on the ground that he in turn would be liable as first indorser, is answered by saying that that defence of avoidance of circuity of action is not available, inasmuch as the circumstances of the indorsement show that the anomalous indorser was not to hold the payee.¹ Professor Ames, in his summary,² states it more simply: "The payee as holder, may obviously indorse the instrument to the surety without recourse, and may also fill up the blank indorsement of the surety to himself. In this way the parties are placed in the same position as if the maker had, in the first instance, delivered the note to the payee, the payee had then indorsed it without recourse to the surety, and the surety had then indorsed it to the payee. In both cases the payee, as second indorsee, charges the surety as second indorser." It has been hinted as an objection to this, that the payee has no authority to indorse "without recourse;" but the answer is that it is not a question of having authority at all. The payee is allowed to bring out matter which will prevent the anomalous indorser from setting up the defence of circuity of action; and indorsement "without recourse" is nothing more than a convenient way of putting down this result. And if it be said that this is really introducing parol evidence to vary a written contract, the answer is that it is not a matter of evidence: the payee may bring in under an equitable defence the same matter which, before the introduction of equitable defences, would have entitled him to an injunction preventing the anomalous indorser from suing him as first indorser; and, certainly, he may prove his case.

Settling ourselves down, then, upon the fact, as it seems proper we may, that the payee as second indorsee may hold the surety as second indorser, and remembering also

¹ *Moore v. Cross*, 19 N. Y. 227 (1859).

² *Ames, B. & N.*, 838.

that notice is necessary to charge an indorser, we are in a fair way to examine the cases with some sense. Our first refreshing surprise is to find how few and of what sort the authorities are; in perhaps not more than four cases was the question involved and in those the discussion is not apt to meet with approval.

In every other case there is something distinguishable. In the cases in which there was no demand or notice it was proper not to hold the defendant. Such were *McCune v. Taylor*,¹ and *Barto v. Schmeck*.² Such, probably, we may also take *Schollenberger v. Neff*,³ and *Fegenbush v. Lang*,⁴ to be from the mere fact that it does not appear that there was notice, and although the defendants in both cases were held, the result is unsatisfactory and must be due to starting with the mistaken notion that guaranty is the proper action. In *Shenk v. Robeson*,⁵ and *Jack v. Morrison*,⁶ nothing is said about notice. The second simply decides that a mere indorsement is not sufficient writing to satisfy the statute. In all these cases excepting *Shenk v. Robeson*, the action was on a guaranty and any discussion in them would have little weight in an action on an indorsement. Even had there been notice, it would have been a sufficient answer to say that plaintiff has misconceived his action. One case—*Smith v. Kessler*⁷—did say that upon indorsement *alone*, the surety is not liable to the payee. Of course, the payee must meet the defence of avoidance of circuity of action and so the burden is upon him to show that the surety was not to have recourse to him.

In only one case before *Schafer v. The Bank*,⁸ does it appear that the defendant had notice, and in that he was held liable to a holder who took from the payee after maturity.

¹ 11 Pa. 460 (1849).

² 28 Pa. 447 (1857).

³ 28 Pa. 189 (1857).

⁴ 28 Pa. 193 (1857).

⁵ 2 Grant, 372 (1858).

⁶ 48 Pa. 113 (1864).

⁷ 48 Pa. 142 (1863).

⁸ 59 Pa. 144 (1868).

Inasmuch as the holder took the note subject to equities, the case practically decides that payee may recover.¹

This, then, is the state of the authorities when we come to *Schafer v. The Bank*,² which is considered the leading case—a distinction due, however, not so much to its solid reasoning and faithful examination of the cases as to its presumptuousness in putting itself down as settling the question for all time. Solomon Schafer was the indorser of a note payable to Jacob and Joseph Schafer. The payees, having indorsed below Solomon Schafer's name, had the note discounted at the plaintiff bank, and it was held that plaintiff could not recover, although there was demand and notice. There were two counts—the first was on guaranty; the second charged defendant as second indorser, alleging that payees were first indorsers.

Justice Sharswood was anxious not to depart from the authorities. "Our unanimous conclusion," he says, "is to adhere to these decisions," and he overruled the only case (*Kyner v. Shower*) that was on all fours with the one he was deciding. He goes on, "But were there more doubt as to the soundness of the principle settled in *Barto v. Schmeck* and *Jack v. Morrison* than there is, we ought not now to depart from them," not recognizing that not only demand and notice distinguished the cases, but that those cases were on actions of guaranty, while here there was a count on the indorsement. This failure to apprehend the subject clearly is noticed also in the examination of the cases. *Taylor v. McCune* and *Barto v. Schmeck* and other cases do not have their decisions stated with the exactness we should expect. It is more than doubtful, too, if Justice Sharswood is justified in his criticism of Justice Gibson's remarks in *Kyner v. Shower*. The statement in that case—"and when there is no such proof, he authorizes the payee to write over his name any form of engagement he may see proper"—may be fairly interpreted to be nothing more than a statement of what Justice Gibson himself conceived the law to be rather than a statement of what he supposed *Taylor*

¹ *Kyner v. Shower*, 13 Pa. 144 (1850).

² 59 Pa. 144 (1868).

v. *McCune* established. And although it may not be quite accurate, its aspect is considerably altered when it is read in the light of the facts of *Kyner v. Shower*.

From Justice Sharswood's whole discussion it is evident that the case was practically decided on the first count, and that it was assumed that there was no liability on the second. It may be worth while to look into the reason for this assumption. We find, in the first place, that it is traceable in some measure to the introduction of presumptions that seem to serve no purpose but that of confusing the subject. In *Taylor v. McCune*, Bell, J., says of *Tillman v. Wheeler*,¹ which he considers decisive of his case, that it decided that "there was nothing to disprove the legal presumption flowing from the appearance of the paper; that T. put his name to it as second indorser, on the responsibility of the payee, and for the accommodation of the drawers and payee, as first indorser." In this case and its partner, *Herrick v. Carman*,² it did not appear that the indorser intended to be anything more or less than a second indorser, with the privileges that go with that position, one of which is to look back to the payee as first indorser. In other words, the payee did not show that there were circumstances which would deny the right of the surety to have recourse to him. There was not this difficulty in *McCune v. Taylor*, for there it appears that Taylor indorsed to give the note credit with the payee; and, therefore, the New York cases were not in point. When nothing appears except the indorsement, it is hard to see what need there is for a presumption; when, on the other hand, it appears that the indorsement was to give credit with the payee, it is contrary to the fact to say that the surety is presumptively a second indorser *upon the responsibility of the payee*. The significant result—and it is perhaps traceable to this misapplication of the New York cases—is that Pennsylvania, while pretending to follow New York, has reached an opposite result—New York having found no difficulty what-

¹ 17 Johns. 325 (1820).

² 12 Johns. 159 (1815).

ever, consistently with *Tillman v. Wheeler* and *Herrick v. Carmam*, in holding the surety.

Another notion that has helped along this assumption that a surety cannot be held, was introduced in *Barto v. Schmeck*. Woodward, J., says: "There was no proof to charge Barto with liability to the payee, and he could be made liable to Schmeck as a subsequent holder only by the payee's assuming the responsibility of first indorser. . . . It was a fraud on Barto, therefore, for Mannerback (the payee) to indorse below him and to negotiate the note to Schmeck without himself assuming the responsibility of a first indorser. And Schmeck took the note, with his eyes wide open to the fact that Mannerback was the payee and could not regularly be second indorser. This was a circumstance sufficient to discredit the commercial character of the paper and to put Schmeck upon inquiry," etc. The court thought that Mannerback was not first indorser, because he signed below Barto; but is the position of the names to determine whether or no one is a first indorser? It seems it ought to be immaterial on what part of the paper the payee writes his name so long as he puts it down as a first indorsement. In other words, is it not simply a question of what was the payee's intention when he indorsed? It seems so; and hence that intention becomes a matter of inquiry for us. Now, it is surely not easy to impute one or another definite intention to a payee who has indorsed below the anomalous indorser, when we know that he indorsed in a half-mechanical way, as a matter of course in business, without any contemplation of the legal refinements that are likely to arise. On the other hand, however, it is not positively stupid for us to say that he meant his indorsement to be an indorsement, and hence meant it to pass legal title and to make a contract just as other indorsements do. But a payee can transfer legal title only by becoming first indorser, for the reason that otherwise a subsequent holder does not come within the tenor of the bill; and, therefore, the fair and natural interpretation of his act is that he did become first indorser.

A further objection to Justice Woodward's dictum is the disastrous result that would come from following it out logi-

cally. If it is to put a purchaser on inquiry when the payee's name is below that of the anomalous indorser, why not when his name is written across the face or lengthwise on the back, or in any other of the numerous positions that may be imagined? To put him on inquiry in a particular case seems nothing less than arbitrary. And what would the result be but to lessen the freedom of currency of negotiable instruments, while the drift of the law merchant is in the opposite direction.

Sharswood, J., of course, had to admit that if the payee indorsed "without recourse" above the surety, then, as to *bona fide* holders, the surety would certainly be conclusively bound to answer as second indorser; but he claimed that, "if the surety was sued by the payee in the character of subsequent indorser, he undoubtedly could show that in fact such restricted indorsement was not made until after he had signed, and, as to any liability to the payee, it may well be questioned whether it would not be a mere evasion of the statute that was intended to prevent perjuries as well as frauds." According to this the *bona fide* holder may sue the surety, who will then have no recourse to the payee as first indorser "without recourse," or he may sue the payee, who, we may suppose, has also signed as third indorser, and the payee cannot hold the surety; so that it is to depend entirely upon the holder, who is to pay the note—the surety or the payee. The trouble seems to be that Justice Sharswood fixes the liability of the surety to the holder by the law merchant (not incorrectly); but when he comes to the liability of the surety to the payee (as second indorsee), he brings in the statute—for what reason it is not easy to understand.

Only two cases can be said in any way to follow *Schafer v. The Bank*. With the admission in *Murray v. McKee*,¹ that "it was rightly decided if *Jack v. Morrison* is to be considered law" there could, of course, be no other conclusion. The other case is *Hauer & McNair v. Patterson*,² in which Sharswood with fatal consistency held that an anomalous indorser

¹ 60 Pa. 35 (1868).

² 84 Pa. 274 (1877).

who took up a note could recover against the payee as first indorser, a conclusion the very opposite of which a good case, *Moore v. Cross*¹ says no one would doubt.

The last case, *Arnot v. Symonds*,² on anomalous indorsement may be consistent with *Schafer v. The Bank*, but the test which it adopts goes far toward relaxing the doctrine of that case. When Arnot purchased the note the payee's name appeared in the proper place on the back, while that of the anomalous indorser was at the opposite end and inverted with respect to the payees'. It was held that the holder could recover against the anomalous indorser. The court says, "If the defendant, in case he is required to pay, will have recourse to the payees, it follows that he is liable as second indorser to the holder. Whether he would have such recourse or *not* is really the test of liability. . . . The legal effect of placing their (the payees') name where it is, is to make them liable as first indorsers." This test has the advantage of doing away with the subject of inquiry and notice which we have seen occasioned some confusion in the earlier cases. Suppose, for instance, a payee comes to A with a note he has not yet indorsed, but upon which there appears the name of the anomalous indorser, then indorses the note above the anomalous indorser and gets the money from A. According to the test laid down here A may recover, even though he has had notice of the character of the indorsement. But, however satisfactory the test may be in such a case, the objection to it is that it will not work where the payee indorses "without recourse" above the name of the surety; for the surety will not then have recourse to the payee, and yet it can hardly be doubted that he would be liable to a *bona fide* holder. A further objection to the reasoning in this case is the arbitrariness with which the rule is laid down that the liability of the indorser depends upon the position of the payee's name. That is, if the payee indorses in position A, the surety is to be held; if one or two inches from position A, he is not to be held. When recovery thus becomes a matter of inches it seems you are

¹ 19 N. Y. 227 (1859).

² 85 Pa. 99 (1877).

getting pretty close to the borderland of absurdity. But besides this there is the difficulty in applying such a rule. Suppose the payee's name were below that of the surety, but in the right direction, while that of the surety is inverted, or suppose payee wrote his name lengthwise along the back, will the test help you very much in determining whether or no payee is first indorser? The simple and workable rule is to say that it is immaterial where payee writes his name; however inartistic its position with reference to other names, it is still a first indorsement if meant to be such.

We have noticed that it seemed improper and confusing in such cases as *Barto v. Schmeck* and *Schafer v. The Bank* to say that the position of the name of the first indorser below that of the second was sufficient to put plaintiff upon inquiry. A case—*Loosee v. Bissell*¹ now came up in which that question would seem, upon first blush, to have been correctly introduced. The payee of a note that had been indorsed by an anomalous indorser pledged the note as collateral security with the plaintiff bank, but did not indorse it; subsequently he had it discounted by the bank and then indorsed it. The bank was not allowed to recover on the ground that the facts were sufficient to put it upon inquiry. Of course, a transferee of a note is taken to have notice of what appears on the note, and in that sense it can, indeed, be said that the holder here was put upon inquiry. But that inquiry would develop the fact merely that the transfer of the note without indorsement of the payee would operate only as an assignment of the payee's interest, and that that interest from the very face of the paper could be nothing more than a right against prior parties. In other words there was no assignment in any sense of any right—legal or equitable—against the surety, and it is irrelevant, therefore, to bring in any talk of notice of equities that he may have against the payee. More than this, it seems quite inaccurate to speak of the equities of the subsequent holder against the payee. An indorser always recovers on his legal title and the question strictly is not whether he has

¹ 76 Pa. 459 (1874).

an equity against the payee, but whether the payee has an equitable defence to the legal action. The defence to plaintiff's action here was *not* that he had *notice*, but that he had not given *value*. The money that he paid in the first instance was in consideration of what was then assigned him, and at that time he got no right against the surety. True, the subsequent indorsement by the payee gave him legal title, but at that time he gave no value for the right, and hence is not a purchaser for value.

A few more cases are usually cited under the head of anomalous indorsement that have no business to be. *Eilbert v. Finkbeiner*¹ merely decides that you may prove a guaranty if you have a writing. In *Temple v. Baker*,² the question was simply whether there was a memorandum in writing sufficient to satisfy the statute.

In *Slack v. Kirk*,³ the discussion of anomalous indorsement with the subsequent supposedly necessary adherence to *Schafer v. The Bank*, gives an awkwardness to the case from which it ought to be free. Slack, the payee, indorsed the note as first indorser. Subsequently, Kirk indorsed the note, but inadvertently wrote his name above that of the first indorser. It was held that Kirk, who when the note fell due paid half of it to the subsequent holder, could not recover from Slack. The theory of the court was that Kirk could be subrogated to the rights of the holder and so recover from Slack, while Slack could not hold Kirk because Kirk was an anomalous indorser. The result was satisfactory; the theory, rather otherwise; for the case seems capable of the simple explanation that a second indorser may hold a first. The contention that this is not so when the name of the second appears above that of the first seems so weak that one hardly stops to consider it. If an answer were needed it would be sufficient to say that it can be shown by parol matter that the second indorser put his name above by mistake.

The latest case cited under anomalous indorsement is *Cen-*

¹ 68 Pa. 243 (1871).

² 125 Pa. 634 (1889).

³ 67 Pa. 380 (1871).

*tral National Bank v. Dreydoppel.*¹ A note was made by J. & E., payable to their own order, and indorsed by defendant, and subsequently by the makers themselves. The court accounts for the refusal of the cases to allow recovery against the anomalous indorser on the ground that he had no recourse to the payee; but it contends that the reason fails in the present case because he has recourse to the payees as makers, and that he should therefore be held. Again the result is correct, but again the question of anomalous indorsement has no business to be discussed. A man cannot promise himself, and so a note payable to the maker is incomplete—is not a note and does not become such until after the maker indorses it. At that time the effect of the indorsement is to make a contract with the indorsee and so complete the note.² This indorsement, however, is not a strict indorsement, for that is a transfer or pre-existing liability, and here there is no such liability. The maker, by putting his own name down as payee, reserves the designation of the payee for a future time and his subsequent indorsement is merely this designation of the payee; so that the apparent anomalous indorser is really the first indorser, and hence there is nothing irregular about the note.

I have gone into the cases sufficiently, I think, to show that they are, at least, not very satisfactory. In not one of them does there seem to be a clear apprehension of the subject; in most of them anomalous indorsement did not require discussion; in those that it did the reasoning could be sounder. And it is more than just possible, too, that it may be fairly said that it has really not been settled in Pennsylvania that an anomalous indorser who gets notice cannot be held. It is certain, at any rate, that the authorities are in such a shape that *stare decisis* loses much of its nightmare effect. That principle, after all, it may sometimes be only the next best thing to follow with conscious blindness; the *very* best thing may be to disregard it intelligently.

George Stern.

Philadelphia; March, 1899.

¹ 134 Pa. 499 (1890).

² *Hooper v. Williams*, 2 Exch. 18.